CPP ANNUAL USE OF CAPITAL SURVEY - 2010

NAME OF INSTITUTION
(Include Holding Company Where Applicable)

Heritage Commerce Corp

Point of Contact:	Larry McGovern (408-494-4562)	RSSD: (For Bank Holding Companies)	2209553
UST Sequence Number:	55	Docket Number: (For Thrift Holding Companies)	
CPP/CDCI Funds Received:	40,000,000	FDIC Certificate Number: (For Depository Institutions)	
CPP/CDCI Funds Repaid to Date:		Credit Union Charter Number: (For Credit Unions)	
Date Funded (first funding):	November 21, 2008	City:	San Jose
Date Repaid[1]:	N/A	State:	California

[1]If repayment was incremental, please enter the most recent repayment date.

American taxpayers are quite interested in knowing how banks have used the money that Treasury has invested under the Capital Purchase Program (CPP) and Community Development Capital Initiative (CDCI). To answer that question, Treasury is seeking responses that describe generally how the CPP/CDCI investment has affected the operation of your business. We understand that once received, the cash associated with TARP funding is indistinguishable from other cash sources, unless the funds were segregated, and therefore it may not be feasible to identify precisely how the CPP/CDCI investment was deployed or how many CPP/CDCI dollars were allocated to each use. Nevertheless, we ask you to provide as much information as you can about how you have used the capital Treasury has provided, and how your uses of that capital have changed over time. Treasury will be pairing this survey with a summary of certain balance sheet and other financial data from your institution's regulatory filings, so to the extent you find it helpful to do so, please feel free to refer to your institution's quarterly call reports to illustrate your answers. This is your opportunity to speak to the taxpayers in your own words, which will be posted on our website.

What specific ways did your institution utilize CPP/CDCI capital? Check all that apply and elaborate as appropriate, especially if the uses have shifted over time. Your responses should reflect actions taken over the past year (or for the portion of the year in which CPP/CDCI funds were outstanding).

X Increase lending or reduce lending less than otherwise would have occurred.

During 2010, the Company made total loan commitments of $510 million, representing $99 million in commitments for new loans and $411 million in renewed loans.

X To the extent the funds supported increased lending, please describe the major type of loans, if possible (residential mortgage loans, commercial mortgage loans, small business loans, etc.).

SBA loan originations totaled $16.3 million in 2010.

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X **Increase securities purchased (ABS, MBS, etc.).**

During 2010, the Company had net purchases of $125.0 million of agency mortgage-backed securities during 2010.

☐ **Make other investments.**

☐ **Increase reserves for non-performing assets.**

X **Reduce borrowings.**

The Company reduced its securities sold under agreement to repurchase from $20.0 million to $5.0 million during 2010.

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☐ **Increase charge-offs.**

☐ **Purchase another financial institution or purchase assets from another financial institution.**

☐ **Held as non-leveraged increase to total capital.**

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What actions were you able to avoid because of the capital infusion of CPP/CDCI funds?

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What actions were you able to take that you may not have taken without the capital infusion of CPP/CDCI funds?

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Please describe any other actions that you were able to undertake with the capital infusion of CPP/CDCI funds.

The Company received $40 million in CPP funds in November 2008, of which the Holding Company downstreamed $20 million of the proceeds to the Bank. The Company had $1.25 billion in total assets at 12/31/10. The Company made total loan commitments of $1.29 billion, representing $289 million in commitments for new loans and $1.00 billion in renewed loans from the time of receipt of the CPP funds on November 21, 2008 through the end of 2010. During 2010, the Company made total loan commitments of $510 million, representing $99 million in commitments for new loans and $411 million in renewed loans. Total loans outstanding decreased from $1.07 billion at December 31, 2009 to $846 million at December 31, 2010 due the timing of funding loan commitments, net charge-offs, loan payoffs, principal paydowns, and the sale of problem loans. However, the Company also made net purchases of $125.0 million of agency mortgage-backed securities during 2010 for its investment securities portfolio to replace the loan runoff. The CPP funds permitted the Company to absorb deterioration in its loan portfolio and remain "well-capitalized" until it was able to complete a private placement of convertible preferred stock for $75 million in the second quarter of 2010 which significantly improved the Company's regulatory capital ratios and thus improved its financial position. While accomplishing the capital raise to improve its financial position, the Company was able to continue lending as described above. The $1.29 billion in loan commitments, made from time of the receipt of the CPP funds until the end of 2010, was primarily to small business and nonprofit organizations which helped employment and people in need, and supported the communities the Company serves in the San Francisco Bay Area. Additionally, by purchasing the agency mortgage-backed securities, the liquidity of such mortgage market was enhanced. As a result of the private placement, capital ratios substantially exceed regulatory requirements for a well-capitalized financial institution, both at the Holding Company and the Bank. The leverage ratio at the Holding Company was 14.1%, with a Tier 1 risk-based capital ratio of 19.7%, and a total risk-based capital ratio of 20.9% at December 31, 2010. The leverage ratio for the Bank was 12.1%, with a Tier 1 risk-based capital ratio of 16.8%, and a total risk-based capital ratio of 18.1% at December 31, 2010. The regulatory "well-capitalized" guidelines are a minimum of a 5% leverage ratio, a 6% Tier 1 risk-based capital ratio, and a 10% total risk-based capital ratio. The Company's earnings, credit quality, capital and liquidity positions, and overall financial condition have significantly improved since the second quarter of 2010. The Company achieved profitability in the third and fourth quarters of 2010 and in the first quarter of 2011, with net income allocable to shareholders of $458,000, $1.1 million and $985,000 for the respective quarters. With the capital raise and improved financial condition, the Company anticipates that it will be able to become current on its deferred dividend payments on the CPP funds in 2011. It should (or could) also enable the Company to repay all CPP funds within a reasonable period of time generating a profit for the CPP. The CPP was an important capital event for the Company, which helped it to continue lending to small to medium sized privately owned businesses in 2009 and early 2010, until the additional capital was raised. Now, with its strong capital position, the Company is in excellent position to lend to a greater number of businesses in its community, which should help those companies add employees and ultimately, improve the economy.